BT Wholesale Focus Australian Share Fund

ARSN: 113 232 812

About the Fund

The BT Wholesale Focus Australian Share Fund (**Fund**) is a highly concentrated portfolio of 15-30 ASX listed stocks, developed to meet investor demand for a higher alpha, higher tracking error fund.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes), that significantly exceeds the S&P/ASX300 Accumulation Index over the medium to long term. The suggested investment timeframe is five years or more.

Investment approach

BTIM aims to add value primarily through active stock selection. The Fund is managed using the same core investment style as is applied to BTIM's other Australian equity portfolios and utilises the team's proven research and stock selection capabilities.

BTIM's investment process for shares is based on our core investment style and is unrestricted by a growth or value bias.

Fund Positioning

The Fund is designed to complement a conventional, core share portfolio by providing satellite exposure to selected Australian equities with the potential for performance enhancement.

Investment Team

BTIM's twenty-six member Equity Strategies team is one of the largest in the Australian fund's management industry. The portfolio manager for the Fund is Crispin Murray, who has more than 26 years' industry experience. Crispin is also Head of Equity Strategies.

Other Information

Fund size (as at 31 Dec 2017)	$363 million
Date of inception	April 2005
Minimum investment	$25,000
Buy-sell spread[1]	0.50% (0.25%/0.25%)
Distribution frequency	Half-yearly
APIR code	RFA0059AU

Investment Guidelines

Ex-ante tracking error	4.5% - 8.0%
Max absolute stock position	15%
Min/max sector position relative to index	+/- 15%
Min/Max BARRA style factors	+/- 0.5 SD
SIRA style factors	Within 1 SD
Maximum cash level	30%
Shorting	No
Borrowing	No

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	2.30	2.41	1.86
3 months	7.78	7.99	7.74
FYTD	9.39	9.93	8.60
6 months	9.39	9.93	8.60
1 year (pa)	16.36	18.03	11.94
2 years (pa)	12.09	13.02	11.86
3 years (pa)	10.69	11.89	8.76
5 years (pa)	13.21	14.29	10.15

Sector Allocation (as at 31 December 2017)

Energy	6.9%
Materials	22.3%
Industrials	11.7%
Consumer Discretionary	8.9%
Consumer Staples	4.7%
Health Care	6.2%
Telecommunication Services	4.3%
Financials ex Property Trusts	27.7%
Cash & other	7.3%

Top 10 Holdings (as at 31 December 2017)

BHP Billiton Limited	11.2%
Commonwealth Bank of Australia Ltd	9.0%
ANZ Banking Group Limited	7.0%
Qantas Airways Limited	6.4%
Westpac Banking Corporation	5.4%
Metcash Trading Limited	4.7%
Telstra Corporation Limited	4.3%
CSL Limited	4.3%
JB Hi-Fi Limited	3.3%
Caltex Australia Limited	3.3%

Management Costs[2]

Issuer fee[3]	0.75% pa
Performance fee[4]	15% x the Fund's performance (before fees) in excess of the performance hurdle.

[1] The buy-sell spread represents transaction costs incurred whenever you invest or withdraw funds, and may vary from time to time without notice.

[2] You should refer to the latest Product Disclosure Statement for full details of fees and other costs you may be charged.

[3] This is the fee we charge for overseeing the operations of the Fund and managing the assets of the Fund. The Issuer fee is paid from the assets of the Fund and is reflected in the unit price of your investment.

[4] The Fund's performance fee is 15% of the Fund's performance in excess of the performance hurdle. The performance hurdle is the performance of the benchmark (S&P/ASX 300 Accumulation Index) plus the issuer fee of 0.75% pa. If a performance fee is payable, it is charged in addition to the issuer fee. The fee is calculated each Business Day based on the investment performance and value of the Fund on that day. If we are entitled to a performance fee, it is paid to us as at 30 June each year.

Risks

An investment in the Fund involves risk, including:

- **Market risk**: The risk that factors affecting one or more countries that can influence the direction and volatility of an overall market, as opposed to security-specific risks.
- **Security specific risk**: The risks associated with an individual security.
- **Concentrated portfolio risk** - The Fund's investment strategy of seeking to generate high returns by investing in a concentrated portfolio of Australian shares makes the Fund more volatile than a diversified Australian share fund.

Please read the Fund's Product Disclosure Statement (**PDS**) for a detailed explanation of each of these risks.

Market review

The domestic equity market finished the calendar year on an upbeat note in December, with the S&P/ASX 300 Accumulation index gaining 1.9% over the month, and 11.9% over CY17. Performance has been particularly strong from Resources (+7.1%/+25.7%), with the help of rising commodity prices over the period; whereas Industrials (+0.7%/+9.2%) also achieved a good return over the 12-month period.

Sector performance was positive in general for December, with the exception of Utilities (-4.5%), Industrials (-0.9%) and Health Care (-0.5%). Energy infrastructure operator, APA Group (APA, -8.6%) gave back all the gains it made in November, and was the largest detractor within Utilities. Its share price has been somewhat range-bound since 2015. Within Industrials, Qantas (QAN, -11.1%) was the worst performer. The national airliner saw its share price retreat amid the soaring oil price over the month. The commodity touched its two-year high as demand continued to firm alongside supply disruptions in Libya and the North Sea. Nevertheless, Qantas' stock performance has been strong at 56.1% over the past 12 months. Finally, the Health Care duo, Cochlear (COH, -5.3%) and CSL (CSL, -1.4%) both declined over the month and weighed on the sector. However, performance has been strong for both companies over the 12-month period, with returns of approximately 42%.

On the other side of the spectrum, Materials (+6.1%) was the best performing sector, as miners continue to benefit from rising commodity prices over the month, with iron ore and copper finishing December at higher levels. As a result, major miners including BHP Billiton (BHP, +8.3%), Rio Tinto (RIO, 6.8%), South 32 (S32, +7.1%) and Fortescue Group (FMG, +6.1%) all recorded solid returns. Outside of these, steel manufacturer Bluescope (BSL, +12.9%) also contributed to sector performance after the company upgraded its earnings guidance for the current fiscal year due to higher steel prices and domestic volumes. It will also benefit from the latest US tax reform, being a partial US dollar earner. Following Materials in terms of index performance contribution was Energy (+6.5%), which benefited from the rising oil price over the month. Woodside Petroleum (WPL, +6.7%), Oil Search (OSH, +11%) and Santos (STO, +7.3%) all managed to record strong gains. Outside of Energy, there were a few notable standout performers including gaming operator Tabcorp (TAH, +15.1%), Tatts Group (TTS, +7.0%) within Consumer Discretionary (+3.7%); as well as Telstra (TLS, +5.8%) and TPG Telecom (TPM, +10.4%) within Telecoms (+5.5%). Tabcorp and Tatts Group made strong gains after the ACCC decided not to review their proposed merger. Tatts Group shareholders approved the proposed merger during the month, which is expected to deliver at least $130 million in earnings synergies. Meanwhile, the Telecoms duo rebounded and recovered some of the losses suffered over the past 12 months.

Finally on global macro developments, investor attention was primarily focused on US developments during the month. This included a 25 basis point interest rate hike by the US Federal Reserve. Committee members also raised their forecast for 2018 Gross Domestic Product (GDP) growth from 2.1% to 2.5% and their inflation estimate from 1.6% to 1.7%. Most major US data during the period was relatively robust including GDP growth of 3.2%, a 0.8% jump in retail sales and a sound 228,000 increase in non-farm payrolls data for November. A long-awaited tax reform proposal also passed both chambers of Congress, which supported global investor sentiment. This was in addition to stopgap measures being passed to keep the government funded into the New Year.

Meanwhile in Europe, the European Central Bank (ECB) maintained its policy settings and President Draghi emphasised the need to keep interest rates at present levels for an extended period, given persistent subdued inflation. On the political front, some uncertainties were felt as the Catalan independence bid in Spain regained its footing and the Italian election date came into sight. In contrast, progress on Brexit negotiations were perceived positively by markets.

Fund performance

The Fund's strong performance in December capped a strong 2017 in terms of both absolute and relative returns. Several of the more non-consensus positions such as Metcash, Santos and JB Hi-Fi drove December's outperformance, while the exposure to resources – primarily via BHP – also made a strong contribution. Qantas and Nine Entertainment detracted, but both remain key drivers of the fund's outperformance over the year.

Contributors

Overweight Metcash

Metcash (MTS, +13.5%) reported its first-half results early in the month, which saw EPS over the period increase by 14.8% compared to the prior corresponding period, as the benefits of its latest Home Timber & Hardware acquisition from Woolworths started to flow through. The Food & Grocery business also performed better than expected on the back of continuous cost reduction benefits from its Working Smarter program, in spite of the negative ex-tobacco sales growth over the prior period. Metcash remains one of our highest conviction stocks. From its half-yearly results, cash flow was evidently strong, whilst the release of inventory from the hardware acquisition demonstrates improved business efficiency. Debts were also brought down meaningfully, reflecting a business with much lower risks when compared to just a few years ago. The fact that the stock is still trading at 13-14x means that the market is yet to fully appreciate the quality of Metcash. With Aldi now approaching the end of its store rollout in WA and SA, and the weak WA economy stabilising, MTS's negative ex-tobacco sales growth is expected to improve from here. That said, we are cognisant that the supermarket industry remains highly competitive.

Overweight BHP

Diversified miner, BHP (BHP, +8.3%) finished December with a strong gain. The outlook for domestic miners remains sanguine for now, with China's supply side discipline continuing to lift commodity prices – both iron ore and copper finished the month higher. The former has now broken through the US$70/mt mark. Going forward, we retain conviction in our BHP position. Considering the strong discipline of capital deployment as well as an asset portfolio with significant scope for further improvement in terms of capital returns, we believe the miner is going to deliver more value to its shareholders in the foreseeable future.

Detractors

Overweight Qantas Airways

National airliner Qantas Airways (QAN, -11.1%) extended its losses in December, finishing the month 11.1% lower amid the surging global oil price. As previously communicated, we remain mindful that if oil prices remain elevated for a sustained period, it can begin to feed through to increased costs and remove some of the expected upside for QAN from here. However, we are not currently at that point and QAN's hedging immunises it against a significant surge in fuel costs in the near term. We believe the recent underperformance was no more than short-term noise, and Qantas remains a key position in our portfolio.

Underweight Woodside Petroleum

As noted above, oil producers enjoyed some buying support during the month, which saw Woodside Petroleum (WPL, +6.7%) advance in December. Our preferred exposures within the space are obtained via Santos (STO, +7.3%) and Oil Search (OSH, +11.0%), both of which also benefited from the rising oil price over the month.

Outlook

Looking into 2018, there are several key issues which we believe should remain at the forefront of investor focus. The first is liquidity, which is no longer providing a tailwind to markets as central banks around the world tighten policy and start to shrink balance sheets. At this point the pace of tightening remains moderate and should allow the market to retain the prevailing valuation rating, however we remain mindful of the risk of over-tightening and keep a watchful eye on this space. We also maintain a close eye on bond yields, given the sensitivity which a large swathe of the Australian market has to changes here. At this point we expect small increases, but not a 'bond bust'. We are underweight bond sensitives as a result, but not heavily so, and have taken advantage of individual opportunities in this sector.

China remains crucial to equity market fundamentals and sentiment and more specifically, for the health of Australia's resource sector. The economic outlook remains stable at this point, with GDP growth expected to continue on its multi-year path of moderate deceleration. The Government remains focused on corporate profitability to help address the country's debt problem and relieve stress on the financial system. The supply-side discipline this entails should continue to support commodity producers.

The most recent Australian reporting season saw a modest tick-up in business capital expenditure which, in combination with population growth and a bulging pipeline of infrastructure projects, should continue to support modest economic growth. This benign environment should continue to underpin corporate earnings.

Perhaps the most significant market factor is the scale and pace of disruption facing a broad swathe of local industries. Whether it is driven by new technology, global competition, or greater political or regulatory intervention, the challenges to incumbent business models and industry structures provides both threats and opportunities for investors. The ability to differentiate between companies within an industry, in terms of their ability to respond to disruption, has been a key driver of our outperformance over the last few years.